ANNUAL REPORT

OF

THE KROGER GROCERY & BAKING COMPANY

FOR THE FISCAL YEAR 1936

Ended January 2, 1937

The Kroger Grocery & Baking Company

Executive Offices: 35 East Seventh Street

CINCINNATI, OHIO

OFFICERS

ALBERT H. MORRILL, *President and General Manager*

CHARLES M. ROBERTSON, *Vice-President and Treasurer*

L. J. HUERKAMP, *Secretary*

J. H. SADLER, *Ass't. Sec'y. and Ass't. Treas.*

F. M. GRIEME, *Assistant Treasurer*

T. S. BURNS, *Assistant Secretary*

J. M. MARKLEY, *Assistant Secretary*

DIRECTORS

R. G. CLARK, Cincinnati
Vice-President and General Manager, Piggly Wiggly Corporation

WALTER A. DRAPER, Cincinnati
President, The Cincinnati Street Railway Company

CHARLES W. DUPUIS, Cincinnati
President, The Central Trust Company

HARRY J. GILLIGAN, Cincinnati
John J. Gilligan & Son

G. A. GINTER, Cincinnati
Member Firm, Nichols, Morrill, Wood, Marx & Ginter

JOHN M. HANCOCK, New York
Partner, Lehman Brothers

L. J. HUERKAMP, Cincinnati
Secretary, The Kroger Grocery & Baking Company

CHESTER F. KROGER, Cincinnati
Capitalist

FRED LAZARUS, JR., Columbus
Vice-President & Treasurer, The F. & R. Lazarus & Co.

JAMES O. MCKINSEY, Chicago
Board Chairman, Marshall Field & Co., Inc.

ALBERT H. MORRILL, Cincinnati
President, The Kroger Grocery & Baking Company; Piggly Wiggly Corporation

CHARLES M. ROBERTSON, Cincinnati
Vice-President and Treasurer, The Kroger Grocery & Baking Company

JOHN R. RONEY, Chicago
Capitalist

PUBLIC AUDITORS

Lybrand, Ross Bros. & Montgomery

GENERAL COUNSEL

Nichols, Morrill, Wood, Marx & Ginter

TRANSFER AGENTS

The Provident Savings Bank and Trust Company, Cincinnati

Bankers Trust Company, New York

REGISTRARS

The Central Trust Company, Cincinnati

The Commercial National Bank and Trust Company of New York, New York

February 10, 1937

To the Shareholders of

The Kroger Grocery & Baking Company:

This report is for our fiscal year 1936, which began on December 29, 1935, and ended on January 2, 1937, consisting of 53 business weeks. Your company operates on a fiscal year having 13 periods of four weeks each. Each year a day or two is lost. This loss must be made up every five or six years by the addition of an extra week. In 1936, this addition was made, thus making that fiscal year one week longer than the normal fiscal year. You will find that in some of the comparisons made between 1936 and 1935, an attempt has been made to reduce the 1936 figures to 52 weeks' results, thus giving a more accurate comparison.

While this report is for the year 1936, it should contain some reference now, rather than a year later, to the unprecedented flood that swept down the Ohio Valley two weeks ago through the central part of the territory served by your company. At the moment when this report is dictated, February 3, the crest of the flood, from Pittsburgh to the Mississippi, has either passed or is about to pass. The worst is over, but the period of rehabilitation will extend for weeks or months. The financial loss to your company, both in damage to property and in cessation of operations has been large. But it has not impaired its resources and we believe it will not seriously reduce the earnings for the first and second periods (January and February) of 1937 as compared with the first and second periods (January and February) of 1936, because the increased earnings of those branches not affected by the flood largely will offset the loss from flood.

Losses were suffered from Huntington, West Virginia, down through Portsmouth and Cincinnati, Ohio, into and beyond Louisville. At Cincinnati our warehouse and factory, never before touched by high water, have been out of commission for ten days but are resuming normal operations today. In Louisville, our one-story warehouse and bakery, heretofore above the highest flood on record, contained, at the crest, four feet of water. The bulk of our loss will be due to the merchandise injured at Louisville. That warehouse will be in operation in the course of the next forty-eight hours. Ample warning has been had of the flood at Memphis, Tennessee, and Little Rock, Arkansas. We anticipate no loss of merchandise in those areas.

You will be glad to know that in the areas which suffered most, the personnel of your company worked gallantly and tirelessly, under the greatest handicaps, to preserve the assets of your company, and in every locality showed leadership and courage in serving the public, by keeping the channels of distribution open, not only for their own merchandise, but for all the food supply channels of the affected areas. In the home city of your company, Cincinnati, the entire food control of the city was placed in the hands of your officers, and in Louisville, your company was called on in an emergency to do all the purchasing for the Red Cross. We feel that the privilege to serve, thus afforded us, has built large good will for your company.

Public Relations

Public relation activities have increased enormously in the last few years, due to the necessities of the case. Our activities in this line fall into two classes. One, resisting by all proper means discriminatory class legislation, fostered by selfish interests and aimed at the economies of distribution which the chain stores admittedly furnish. The other consists of creating and directing means for bringing to the public, knowledge of the facts and basic economic advantages of the rapid and economical system of distribution maintained by the chains which tend towards higher quality and lower prices.

In the states in which we operate, there are now existing eleven discriminatory tax laws which levy approximately $379,943 of discriminatory taxes annually against your company. Bills are pending in the legislatures of six states where your company operates. For the most part this class of legislation has been enacted during the past three years and has added to our increasing burden of taxation.

I have reported to you before that in my opinion ultimately the urge for the passage of these laws would disappear, for they are essentially class legislation promoted by and beneficial to a small minority of business interests and essentially detrimental to the interests of the community as a whole. We now hear, even from the professional opponents of the chains, that they do not wish to destroy the chains, but only to regulate and burden them. The economic and social advantages of the chains, it seems to us, are slowly permeating even the consciousness of their opponents.

The most striking occurrence in the field of anti-chain legislation during the past year was the repeal by referendum of the California $500 per store chain store tax. The campaign preceding this referendum was extensive and thorough, and proved that when the public understands the services that the chains render it, anti-chain store laws are disapproved.

Acting on the experience and precedent furnished by the California referendum, your company, with cooperation from some other chains, is undertaking to build good will throughout the states where it operates, by a systematic and extensive program of working with and contacting producers, consumers and others. This program involves additional expense, will be slow in producing results, but in the long run we are confident it will materially benefit your company.

One phase of this class of activities, in which all chains have cooperated, constitutes a striking development of the last year. In May of 1936, the canned peach market was glutted at its source of supply and the growers asked the chains to move the over-supply. By united effort not only was the over-supply moved but market prices were stabilized. It was a remarkable demonstration of the ability of the chains to distribute food rapidly and economically. Again in August, the producers of beef cattle; in the Fall, the producers of dried fruit; at the Thanksgiving and Christmas seasons the producers of turkeys; and currently, the producers of grapefruit and lamb, all suffering from an over-production which threatened or threatens to cause a crash in the prices of each commodity, appealed to the chains for cooperative action and distribution. Again in each case, through the united effort of the chains, the acuteness of the situation was entirely relieved. We hope, through this organized effort, to come to the rescue of the producer whenever circumstances justify it, thus demonstrating in practice, and irrefutably, the service which the chain method of distribution renders the producer and consumer.

Directors and Officials There have been no changes in the Board of Directors or among the officers of your company during the last fiscal year.

Sales Total sales for the fiscal year 1936 (53 weeks) amounted to $242,273,498. This figure represents an increase of $12,365,614 or 5.38% over sales of $229,907,884 in the 52 weeks of the fiscal year 1935.

Sales for the first 52 weeks of the fiscal year 1936 showed an increase of approximately 3.5% over sales for the fiscal year 1935 (52 weeks). Average weekly retail sales in the fiscal year 1936 were $1,060 per store as compared with $1,018 per store in 1935, an increase in 1936 of 4.1%.

According to the index published by the Bureau of Labor Statistics, retail food prices in 1936 averaged 2.1% higher than in 1935. An increase in tonnage sales, both in total and per store, is therefore indicated for 1936.

Earnings The attached consolidated income account for the fiscal year 1936 shows, after Federal Income Taxes, final net income of $3,487,831.71. This is equivalent, after preferred dividends, to $1.91 per share on the 1,821,989 shares of common stock, on which dividends are being paid, compared with a final net income for 1935 of $4,110,925.98 or $2.25 per share.

Of the above final net income, $237,444.20 represents dividends received from your company's subsidiary, Piggly Wiggly Corporation.

The decline in earnings in 1936, as compared with 1935, occurred during the first six periods of the year, as reported to you in the semi-annual statement dated June 26, 1936, and resulted in earnings for the first six periods of $0.54 per share. With the beginning of the last seven periods, sales showed a substantial increase, and profits for the last seven periods amounted to $1.37 per share as compared to profits of $0.95 for the last seven periods of 1935.

It is to be noted that earnings for 1935 benefitted by an addition of $0.26 per share, derived not from current operations of that year, but from earnings of previous years, recovered in 1935, because of the invalidity of certain chain store tax laws. Earnings in 1936 received no such benefit.

A comparison of the trend of earnings in the past two years is best shown by the following tabulation.

	1935	1936
First 6 periods, per share............	$1.30	$ .54
Last 7 periods, " "	.95	1.37
Total earnings, " "	2.25	1.91

It is significant that in spite of increased expenses, commented on in the next paragraph, earnings definitely improved in the last seven periods of 1936.

Expenses In all industries in 1936, there was a gradual emerging from the Depression, and in consequence, there was a very definite trend upward of living costs, prices and wages. This upward trend had a very marked effect in increasing our expenses. The increase in imposed burdens, such as Social Security and other taxes, was also a factor.

Operating and Administration Expenses showed an increase in 1936 over 1935 of approximately $1.07 per share. In addition there was an increase in Transportation, Warehousing and Manufacturing wages, equivalent to approximately $0.32 per share, which are included in Cost of Sales, indicating a total increase in expenses amounting to $1.39 per share, of which approximately $1.00 was increased compensation to employees and Social Security taxes.

In 1936, there was a plan of profit-sharing established applicable to many classes of employees, but to no officers, whose success could be gauged directly by profits produced by them. The amount paid to employees, under this plan, and as bonuses and gratuities, amounted to approximately $0.25 per share. It is of interest to compare this amount of profits shared with employees with the extra dividend disbursement made to shareholders, amounting to $0.30 per share. We feel that the trend of the times will continue to require that an equitable and reasonable share of the profits of business be distributed between shareholders and employees.

It will be noted that the disbursements in dividends during the past year amounted to $1.90 a share and the earnings to $1.91 a share, thus avoiding payment of surtax on undistributed profits.

Depreciation As shown by the income account, the company continued substantially the same depreciation policy and rates as in recent years.

Inventories At the beginning of the fiscal year 1936, inventories amounted to $20,129,097. At the end of the fiscal year 1936, inventories amounted to $22,692,864, an increase as of January 2, 1937, over December 28, 1935, of $2,563,767 or 12¾%.

This policy of inventory increase was adopted advisedly in view of the threat of rising prices.

Cash Position The graphs on page 14 illustrate the comparison of cash position and current ratio as of January 2, 1937, as compared to December 28, 1935. The less favorable ratio at the end of the last fiscal year is more than accounted for by the increase in inventories.

Loans On January 2, 1937, your company had no bank loans and has had none to the date of this report since early in 1931.

Capital Structure There have been no changes in the capital structure during the past year. As of January 2, 1937, there were 1,830,885 shares of common stock issued and outstanding. No other capital obligation is outstanding ahead of the common shares except that of $104,100 par value preferred stock.

Shareholders The number of shareholders as of the end of the fiscal year is shown on page 15. During the year the number increased approximately ten per cent, indicating a continuously wider distribution of our stock.

Store Maintenance, Expansion and Closing At the end of the fiscal year 1936, we were operating 4,212 grocery stores, 38 (1%) less than the 4,250 stores operated at the close of the fiscal year 1935.

At the end of 1936, we operated 2,626 meat markets, 27 (1%) less than the 2,653 in operation at the end of 1935.

Last year we reported a continuation of the trend of the last five years towards a smaller number of stores and this trend has continued, although it has flattened out somewhat. It is not the number of stores, but the profitable operation of stores that is important. During 1937 we will probably maintain about the same number of stores as during 1936.

During 1936 your company constructed and is now occupying two new warehouses, complete with coolers and banana ripening rooms, one at Roanoke, Virginia, and one at Peoria, Illinois. A bakery has been established at Pittsburgh, the bakery at St. Louis has been relocated and improved, and bakeries at Louisville and Detroit have been remodelled.

Merchandising and Operations Decentralization of merchandising and operations in progress for a number of years, reached what may prove to be its climax in the early part of 1936. The benefits of this decentralization are only acquired slowly through training and direction. Ultimately, in our opinion, the benefits will be large. Through the period of training and change, which was at its height in 1936, the benefits are still to come, while the expense of the change in organization has actually arrived. We are hopeful that the benefits already apparent will show real results in 1937.

Manufacturing Again we can report an extension of our manufacturing activities. We are constantly adding to the lines of merchandise manufactured, processed and packaged by ourselves, and sold under our increasingly well known labels. The quality and uniformity of these products, and of all of our private label merchandise, has been substantially improved in the last few years through the efforts of our Manufacturing Division, and the rigid inspection and testing done by the Kroger Food Foundation.

Personnel Our attention to and training of personnel, our most valuable asset, has not been relaxed during the past year. We still spend large sums on its direction and instruction. Our turnover has somewhat increased, particularly among our largest single class of employees—store clerks. This is the natural result of improvement in the economic situation. The work in the grocery field, in every class of activity, requires long hours, particularly in the stores. We are constantly striving towards reduction in store hours. A reduction has been obtained in some centers with the cooperation of competitors. Your company can not reduce store hours unless competition does likewise.

At the close of the fiscal year 1936 we had 21,429 employees, compared with 21,611 at the end of the fiscal year 1935.

The fourth year of the Kroger Employees Mutual Benefit Association, operated entirely by employees, showed 92.6% of eligible employees protected by group insurance, provided by this Association. During the year the cost of this insurance was lowered and the benefits increased substantially.

Credit Unions, sponsored by this Association, had during 1936, 10,351 employee members, and cash on deposit at the end of the year of $560,235, of which $492,653 was on loan in small amounts to 5,114 members. The Unions show a loss experience to date of a little less than one-tenth of one per cent a year.

Piggly Wiggly Corporation Piggly Wiggly Corporation, 99% of the stock of which is owned by your company, progressing in 1935 over 1934, made additional progress during 1936. Your company received from this source dividends aggregating $237,444.20 for 1936 as compared to $203,498.40 in 1935.

Subsidiaries Dissolved In June, 1936, to secure unity of operation, and because of Federal Tax Laws, four subsidiary companies, namely, Consumers Sanitary Coffee & Butter Stores, The Kroger Grocery & Baking Company, Inc. (of Virginia), Tennessee Piggly Wiggly Company, and Georgia Piggly Wiggly Company, were dissolved and their assets transferred to the parent company, by authority of the Board of Directors. This action will be submitted to the stockholders for approval. It did not affect the property of your company. It merely placed all store operations under a single unit.

Taxes In 1937, we will carry an additional burden under the Social Security Act. Last year one per cent of the payroll, amounting to $334,888, was charged against current operations. In 1937, approximately 3% of the payroll will be so charged, 2% for unemployment insurance and 1% for old age pensions. In this year, under this law, we will pay about one million dollars, and in 1938, one million, three hundred thousand dollars as compared to $334,888 paid in 1936.

In 1936, total increases in direct tax payments, including Sales and Social Security taxes, amounted to $641,647 over those paid in 1935, or $0.35 per share.

We are glad to acknowledge the valuable service rendered by our capable Board of Directors, each one of whom responds promptly and generously to our requests for advice or services. To our personnel, from the bottom to the top ranks, we extend grateful acknowledgement of their loyalty, industry and faithfulness.

Respectfully submitted,

Albert H. Morrill

President

FOREWORD TO FINANCIAL STATEMENTS

The balance sheet, income account and earned surplus which follow on pages 8 to 11 summarize the accounts of The Kroger Grocery & Baking Company, after consolidating therein the assets and liabilities of the Wesco Foods Company and the Colter Company. In accordance with consistent practice the assets and liabilities of the Piggly Wiggly Corporation are not consolidated therein. The dividends received on the capital stock owned of the Piggly Wiggly Corporation are included in the income account.

The proportion of the undistributed profits accrued on the capital stock owned of the Piggly Wiggly Corporation, a subsidiary not included in the consolidated financial statements, aggregates $55,747.71 since the date of acquisition of the stock in 1928.

It has been the consistent practice for several years to charge operations with the cost of all leasehold improvements when made. Effective as of the beginning of the year 1936, this policy was changed only in so far as concerns permanent improvements to long-lived leased property, used in manufacturing and warehousing. In 1936, the cost of such improvements aggregated $40,278, and in 1936 and subsequent years the cost of these improvements will be amortized over the life of the lease of the respective properties.

A claim for refund of processing taxes has been filed with the Federal Treasury Department. Part of this claim applicable to current operations, approximating $140,000, has been included in the earnings of 1936, which in part offsets the price declines on floor stocks, taken in January, 1936. Actual collections of processing taxes of all kinds subsequent to date of the balance sheet exceed the amount included in the earnings of 1936.

A plan of self-insurance of casualty risks was adopted in November, 1935 and the effect of such plan was in full force for the year 1936. Adequate reserves, estimated on the basis of the claims filed, have been provided to meet any probable losses that might occur. Under the plan substantial savings have resulted as compared with the previous cost of insurance with outside companies.

No liability appears to have been incurred for surtax on undistributed profits of 1936.

The property losses resulting from the recent flood in the Ohio Valley are commented upon by the President of the company in the annual report to the stockholders.

The Kroger Grocery & Baking Co

CONSOLIDATED BALANCE SHEETS, JAN

(The foreword to financial statements

ASSETS	January 2, 1937	December 28, 1935
CURRENT:		
Cash in banks and on hand	$ 9,752,287.60	$10,158,664.22
United States Government securities, at par:		
Held in escrow, $27,500, 1936 and 1935 (Quoted market prices 1936, $27,732.03; 1935, $400,985)	27,500.00	398,000.00
County and municipal bonds, at par:		
Held in escrow, $10,000, 1936 and 1935 (Quoted market prices 1936, $164,620; 1935 $286,709)	164,000.00	281,000.00
Notes and accounts receivable, net of allowance for those doubtful of collection:		
Customers, including welfare associations and relief agencies	$ 683,140.90	$ 1,307,364.23
Employees	10,809.09	8,685.84
Claims, advances, etc.	646,333.78	503,412.81
	$ 1,340,283.77	$ 1,819,462.88
Inventories of merchandise, at lower of cost or market	$22,692,864.27	$20,129,096.98
Prepaid insurance, rent, taxes, etc.	910,492.76	450,898.68
Accrued accounts receivable, not due	144,957.28	210,533.48
TOTAL CURRENT ASSETS	$35,032,385.68	$33,447,656.24
Deferred claims receivable, net of provision for possible losses	$ 204,222.39	$ 365,590.17
Investments, at ledger values:		
Stock of subsidiary company, not included in consolidation, at cost	$ 6,066,899.99	$ 6,066,459.99
Other stocks, bonds, and mortgage notes, etc.	143,355.83	186,049.93
	$ 6,210,255.82	$ 6,252,509.92
Common stock of company held for sale to employees (8,896 shares 1936 and 1935)	$ 97,157.05	$ 97,157.05
Cash and certificates of dividend accumulation held for use and benefit of employees under group insurance plan (Contra)	$ 168,261.30	$ 124,838.41
FIXED ASSETS:		
Land and buildings, as appraised by The American Appraisal Company, Harry S. Cutmore and Associates, C. G. Richardson, C. E., and the real estate department of the company, as at January 1, 1933, with subsequent additions, at cost:		
Land	$ 1,349,503.88	$ 1,389,532.86
Buildings	$ 8,685,735.70	$ 8,723,574.92
Machinery and equipment, as appraised by The American Appraisal Company, as at January 1, 1933, with subsequent additions, at cost	17,097,132.89	16,323,654.05
Automotive equipment, etc., at cost	3,404,575.45	3,036,254.81
	29,187,444.04	28,083,483.78
Less, Allowance for depreciation and obsolescence	14,839,732.58	13,803,524.52
	$14,347,711.46	$14,279,959.26
TOTAL FIXED ASSETS	$15,697,215.34	$15,669,492.12
Store and general supplies and deferred charges to future operations	$ 562,296.77	$ 514,329.94
	$57,971,794.35	$56,471,573.85

...pany and Subsidiary Companies
...ARY 2, 1937 AND DECEMBER 28, 1935
(... an integral part of this balance sheet)

LIABILITIES		January 2, 1937		December 28, 1935
CURRENT:				
Accounts payable, vendors, etc.		$ 5,338,329.71		$ 4,450,785.07
Accrued expenses, taxes, etc.		2,072,814.47		1,381,603.37
Provision for federal taxes, current and prior years		886,068.52		1,062,936.12
Dividends payable		887.00		1,722.50
TOTAL CURRENT LIABILITIES		$ 8,298,099.70		$ 6,897,047.06
Provision for self insurance		248,657.81		145,934.32
Provision for rentals of closed stores, not yet due		183,329.84		249,630.97
		$ 8,730,087.35		$ 7,292,612.35
Amounts due employees representing dividends and premium refunds on group insurance held by company for the use and benefit of employees (Contra)		$ 168,261.30		$ 124,838.41

CAPITAL AND SURPLUS				
Preferred capital stock outstanding:				
First Preferred, 6 pct. par $100		$ 55,700.00		$ 55,700.00
Second Preferred, 7 pct. par $100		48,400.00		48,400.00
		104,100.00		104,100.00
Common capital stock without par value: (Authorized 3,000,000 shares)				
	Shares		*Shares*	
Issued	1,848,278		1,848,278	
Less, In Treasury	17,393		17,393	
Outstanding	1,830,885	33,398,249.80	1,830,885	33,398,249.80
Capital surplus		1,047,760.62		1,047,760.62
Earned surplus, appropriated for contingent uninsured losses		93,161.85		93,161.85
Earned surplus, as annexed		14,430,173.43		14,410,850.82
		$49,073,445.70		$49,054,123.09
		$57,971,794.35		$56,471,573.85

The Kroger Grocery & Baking Company
and Subsidiary Companies

CONSOLIDATED EARNED SURPLUS ACCOUNT

for the period from December 29, 1935 to January 2, 1937

(The foreword to financial statements is an integral part of this surplus account)

Balance, December 29, 1935			$14,410,850.82
Add:			
Net income for the fiscal period ended January 2, 1937, as annexed			3,487,831.71
			17,898,682.53
Deduct:			
Cash dividends paid in the fiscal period ended January 2, 1937:			
First Preferred	$6.00 per share	$ 3,342.00	
Second Preferred	7.00 per share	3,388.00	
Common	1.90 per share	3,461,779.10	
			3,468,509.10
Balance, January 2, 1937			$14,430,173.43

The Kroger Grocery & Baking Company
and Subsidiary Companies

CONSOLIDATED INCOME ACCOUNT

for the periods from December 29, 1935 to January 2, 1937
and from December 30, 1934 to December 28, 1935

(The foreword to financial statements is an integral part of this income account)

	Fiscal period ended January 2, 1937	Fiscal period ended December 28, 1935
Net sales	$242,273,498.21	$229,907,884.36
Cost of sales, including warehousing and transportation expenses	193,102,412.03	182,576,691.42
	$ 49,171,086.18	$ 47,331,192.94
Operating expenses, excluding depreciation	$ 41,367,846.44	$ 39,380,553.70
Administrative expenses	2,043,050.37	2,081,788.56
	$ 43,410,896.81	$ 41,462,342.26
Profit from operations before allowance for depreciation	$ 5,760,189.37	$ 5,868,850.68
Allowance for depreciation	2,365,433.66	2,290,652.60
	3,394,755.71	3,578,198.08
Interest earned, net of interest paid	19,945.66	41,938.09
Profit from operations and other income, excluding income from subsidiary and affiliated sources, unusual income, and before federal income taxes	3,414,701.37	3,620,136.17
Net earnings of subsidiary and affiliated companies for fiscal years (includes dividends of $237,444.20 in 1936 and $203,498.40 in 1935 received from a subsidiary not included in consolidated statements. The proportion of earnings of the subsidiary company accrued on capital stock owned exceeded the dividends received by $4,346.38 in 1936 and $27,785.85 in 1935)	580,330.34	500,512.00
Profit before unusual income and federal income taxes	3,995,031.71	4,120,648.17
Taxes charged against income of prior years and recovered in 1935 because of the invalidity of certain chain store tax laws, less federal income taxes thereon	——	467,450.69
	3,995,031.71	4,588,098.86
Federal income taxes, estimated	507,200.00	477,172.88
Net income	$ 3,487,831.71	$ 4,110,925.98

LYBRAND, ROSS BROS & MONTGOMERY

ACCOUNTANTS AND AUDITORS

CAREW TOWER
CINCINNATI

WILLIAM M LYBRAND
T. EDWARD ROSS
ROBERT H MONTGOMERY
JOSEPH M. PUGH
WALTER A. STAUB
H HILTON DUMBRILLE
JOHN HOOD, JR.
HOMER N SWEET
T B G. HENDERSON
GEORGE R KEAST
PRIOR SINCLAIR
NORMAN J. LENHART
DONALD P. PERRY
WALTER L. SCHAFFER

A. CHARLES GUY
RESIDENT PARTNER

NEW YORK
PHILADELPHIA
CHICAGO
BOSTON
NEWARK
BALTIMORE
WASHINGTON
PITTSBURGH
DETROIT
CLEVELAND
CINCINNATI
ROCKFORD
LOUISVILLE

ST LOUIS
ATLANTA
DALLAS
HOUSTON
SAN FRANCISCO
LOS ANGELES
PORTLAND
SEATTLE

LONDON
PARIS
BERLIN

The Board of Directors,
The Kroger Grocery & Baking Company,
Cincinnati, Ohio.

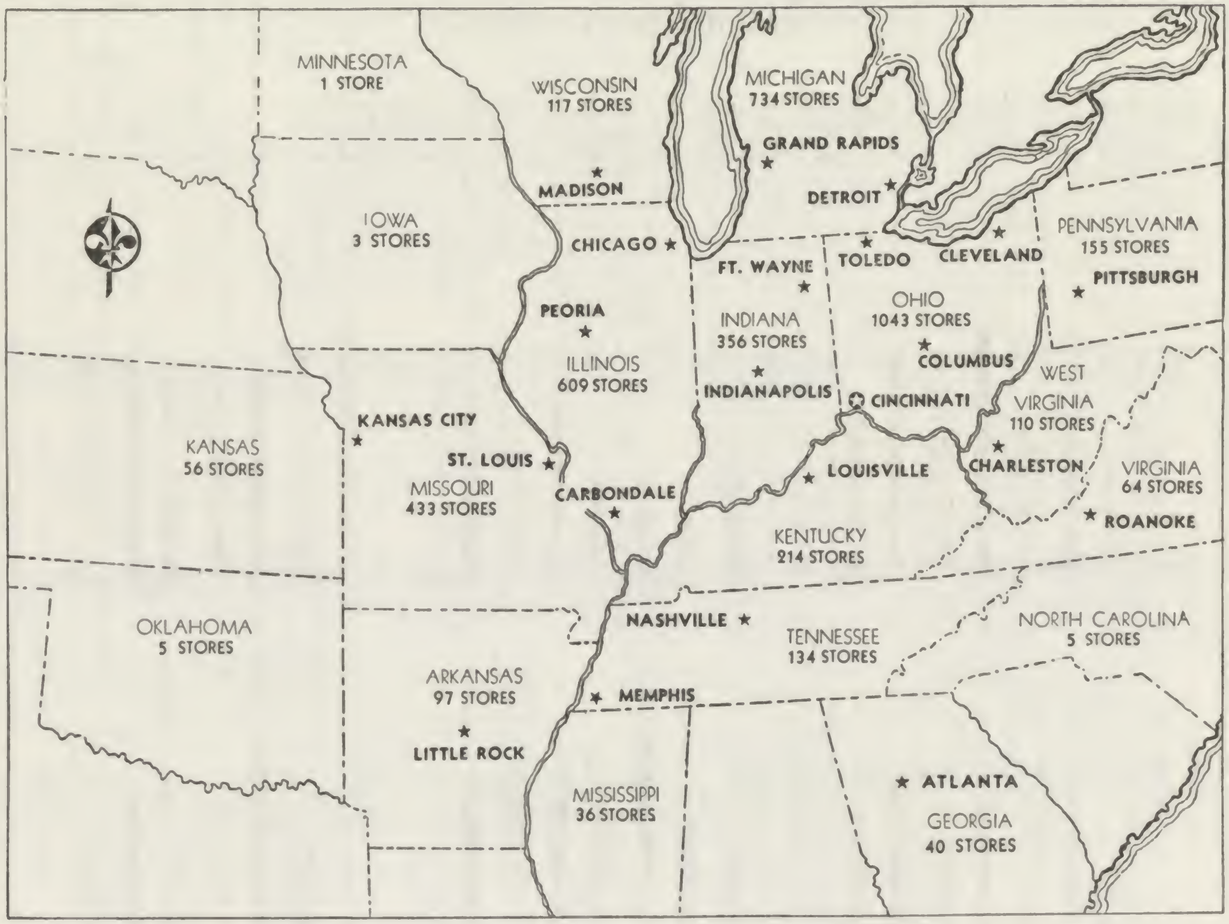
We have made an examination of the consolidated balance sheet as at January 2, 1937 and of the consolidated statements of income and earned surplus for the year 1936 of The Kroger Grocery & Baking Company and subsidiaries. In connection therewith, we examined or tested accounting records of the Companies and other supporting evidence and obtained information and explanations from officers and employees of the Companies; we also made a general review of the accounting methods and of the operating and income accounts for the year, but we did not make a detailed audit of the transactions.

In our opinion, based upon such examination, the accompanying consolidated balance sheet, the related consolidated statements of income and surplus and the foreword to the financial statements fairly present, in accordance with accepted principles of accounting consistently maintained by the Companies during the year under review, their position at January 2, 1937 and the results of their operations for the year then ended.

Lybrand Ross Bros & Montgomery

Cincinnati, Ohio.
February 10, 1937.

MAP OF KROGER OPERATIONS



The map shows the location of branch headquarters cities. In each of these cities a warehouse, a transportation unit and an office are maintained. It also shows the number of stores in operation in each of the nineteen states in which your company was operating at the close of the fiscal year.

In addition to the facilities maintained in branch headquarters cities, subwarehouses, located at strategic points, facilitate distribution to stores in surrounding communities. The company operates one or more stores in each of 1562 towns and cities.

Manufacturing operations are conducted in sixteen cities conveniently located throughout the company's territory.

Bakeries are operated in fourteen cities, namely Chicago, Cincinnati, Cleveland, Columbus, Detroit, Fort Wayne, Grand Rapids, Indianapolis, Louisville, Madison, Memphis, Pittsburgh, Roanoke and St. Louis.

Coffee roasting plants are situated in Cincinnati and St. Louis.

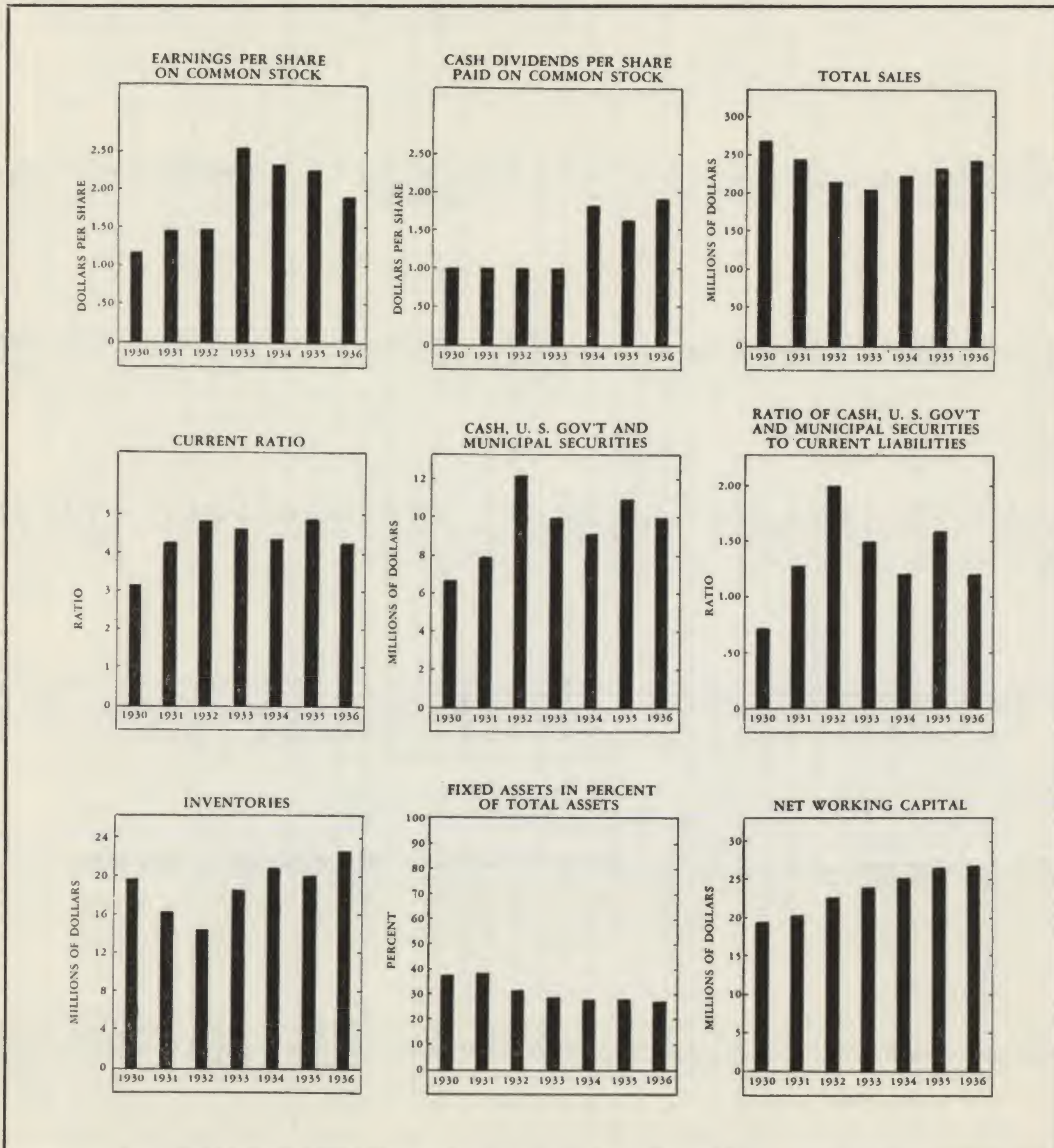
Dairies are operated in Cincinnati, Dayton, Grand Rapids, Indianapolis and Toledo.

A meat distributing and processing plant is located in Cincinnati, and a packing plant is operated in Columbus.

Other manufacturing operations of the Kroger Company include beverage plants, a printing plant, and laundries at suitable locations. In a factory in Cincinnati, various food products are processed and packaged for sale in the company's stores under its brand names. A factory manufacturing store fixtures and equipment is operated at Jackson, Tennessee, by a Kroger subsidiary.

The Kroger Grocery & Baking Company and Subsidiary Companies

FINANCIAL AND OPERATING CHARTS for the fiscal years 1930 to 1936, inclusive



The Kroger Grocery & Baking Company
and Subsidiary Companies

FINANCIAL AND OPERATING STATISTICS for the fiscal years 1930 to 1936, inclusive

	1930	1931	1932	1933	1934	1935	1936
PROFIT AND DIVIDENDS							
Final Net Profit—Dollars Per Sh.*	1.14	1.46	1.47	2.51	2.31	2.25	1.91
—Total Dollars...	2,168,247	2,731,128	2,740,867	4,546,203	4,198,241	4,110,926	3,487,832
Cash Dividends Paid Per Common Share*	1.00	1.00	1.00	1.00	1.80	1.60	1.90
STOCK							
Number Shares Common Stock outstanding with Public—End of Year	1,813,486 6/20	1,813,486 6/20	1,811,091 6/20	1,792,366 6/20	1,810,293 6/20	1,821,989	1,821,989
Number Shareholders—End of Year	16,945	18,856	20,680	19,605	20,633	22,537	24,535
SALES							
Total Sales—Dollars*............	267,094,345	244,371,147	213,159,743	205,691,715	221,175,330	229,907,884	242,273,498
Average Retail Sales—Dollars Per Store Per Week....	954	941	848	861	968	1,018	1,060
Index Numbers—Base, 1930=100:							
Total Sales—Dollars...........	100	91	80	77	83	86	91
Retail Sales Per Store Per Week.	100	99	89	90	101	107	111
Retail Food Prices Bureau of Labor Statistics... (U. S. Dept. of Labor)	100	82	69	67	74	81	82
Tonnage Sales—Total.........	100	111	116	116	111	107	110
—Per Store Per Week	100	120	130	135	136	132	135
STORES							
In Operation at End of Year:							
Grocery.....................	5,165	4,884	4,737	4,400	4,352	4,250	4,212
Meat........................	2,990	2,869	2,845	2,767	2,748	2,653	2,626
Average Number Operated During Year:							
Grocery.....................	5,302	4,980	4,816	4,573	4,356	4,286	4,239
Meat........................	3,033	2,889	2,877	2,815	2,745	2,694	2,655
Licensed Piggly Wiggly Stores At End of Year..............	2,767	2,558	2,143	1,979	1,836	1,544	1,398
EMPLOYEES							
Number Full-Time Employees At End of Year..............	20,072	18,906	18,367	20,872	22,023	21,611	21,429
BALANCE SHEET STATISTICS							
Current Ratio*.................	3.13	4.27	4.81	4.60	4.35	4.85	4.22
Cash, U. S. Government and Municipal Securities:							
Dollars*.....................	6,587,755	7,884,339	12,035,381	9,890,785	9,091,800	10,837,664	9,943,788
Ratio to Current Liabilities*...	.72	1.27	2.00	1.48	1.21	1.57	1.20
Inventories—Dollars*............	19,937,671	16,443,597	14,589,421	18,627,029	20,916,910	20,129,097	22,692,864
Fixed Assets in Percent of Total Assets*......................	38	39	32	29	28	28	27
Net Working Capital*...........	19,583,517	20,278,307	22,920,966	24,138,697	25,202,194	26,550,609	26,734,286

*Shown graphically on opposite page.